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Contracts -- Fraud -- Misrepresentation of State of Mind -- Parol Evidence

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courses are being given by Professor Breck P. McAllister, of the University of Washington.

Professor Frank W. Hanft is teaching the course in Administrative Law this fall at the Duke University School of Law.

Dean M. T. Van Hecke is serving this year as Reporter for the American Law Institute's Restatement of the Law of Injunction against Tort.

Visiting professors during the summer session of 1938 included: Willard J. Graham, of the University of Chicago, who gave the course in Accounting in Law Practice; Harry Shulman, of Yale University, who gave the course in Federal Jurisdiction and Procedure; and Edson R. Sunderland, of the University of Michigan, who taught Trial Practice. A conference on the new Federal Rules of Civil Procedure, in which one hundred and fifty lawyers participated, was held at the Law School on July 12. Discussion leaders were Professors Shulman and Sunderland, U. S. District Judge Johnson J. Hayes, and U. S. Circuit Judge John J. Parker.

NOTES AND COMMENTS

Contracts—Fraud—Misrepresentation of State of Mind—Parol Evidence.

P, a motion picture exhibitor, brought an action of deceit against *D*, a motion picture distributor, to recover damages for an alleged oral misrepresentation which induced *P* to enter into a written contract. The written contract listed a group of motion pictures for release by *D* to *P*, but provided that *D* might substitute other pictures for those listed. The complaint stated that *D*, with the intent not to perform, orally promised to release the pictures listed without exercising his option to substitute. Relying on *D*'s oral promise, *P* signed the written contract, and by *D*'s failure to release such pictures, he has been damaged. On demurrer, *held*, as the written agreement specifically covered the matter in controversy, evidence of a prior oral promise, though fraudulent, is inadmissible; the complaint fails to state a cause of action.¹

The courts define fraud as the representation of a present, material fact, which is known by the maker to be false, and upon which the other

¹ *Oxnard Theatres, Inc. v. Paramount Pictures, Inc.*, 24 F. Supp. 44 (S. D. Cal. 1938). This is one of a series of actions brought by different plaintiffs against the same defendants. The original case is *Blake v. Paramount Pictures, Inc.*, 22 F. Supp. 249 (S. D. Cal. 1938).

party has justifiably relied, and has thereby been damaged.² In general, fraud cannot be predicated on a promissory statement of fact,³ and no tort action may be based on such a promise. As statements of an event to occur in the future, such promises are not representations of present facts, but statements of opinion and are not actionable. However, a promise made with a present intent not to perform, as distinguished from an unperformed promise, raises a more complicated question of law. The majority of courts now recognize the promise in the former circumstance as fraudulent.⁴ They justify this position by implying a representation of a present intent to perform in every promise made. Since intent is a present condition of mind, it is also a present fact. The misrepresentation of that condition of mind is a misrepresentation of a present fact, and, therefore, falls within the definition of fraud—assuming materiality and reliance. The minority of jurisdictions accept a narrower doctrine as laid down by Wigmore,⁵ and refuse to allow fraud to be predicated on any promise, because it is the representation of a future occurrence which ordinarily resolves itself into a statement of opinion or speculation and, as such, is not actionable fraud.

Ordinarily the parol evidence rule will operate to exclude evidence of negotiations prior to or contemporaneous with the execution of a written contract where that evidence will vary, add to, or contradict the terms of the writing.⁶ However, it is well established that evidence of

² *Wheat v. McNiell*, 111 Cal. App. 72, 295 Pac. 102 (1931); *Dallas v. Wagner*, 204 N. C. 517, 168 S. E. 838 (1933); *Prime Mfg. Co. v. Allen-Hough Carryola Co.*, 210 Wis. 72, 245 N. W. 70 (1932); *HARPER, TORTS* (1933) §217.

³ *Burson v. Adamson*, 93 Colo. 301, 25 P. (2d) 723 (1933); *Conger v. Thomas & Lane*, 258 Mich. 702, 242 N. W. 815 (1932); *Jacquot v. Farmers' Straw Gas Producer Co.*, 140 Wash. 482, 249 Pac. 984 (1926); *HARPER, TORTS* (1933) §220.

⁴ The principle that fraud may be predicated on a promise made with a present intent not to perform was first stated by Lord Bowen in *Edgington v. Fitzmaurice*, 29 Ch. D. 459, 483 (1885): "The state of a man's mind is as much a fact as the state of his digestion,—it is more difficult to prove but if there is such a misrepresentation of the state of a man's mind it is as much a misrepresentation as a statement of fact." This doctrine was followed in the United States and has now become the weight of authority. *Knudson v. Domestic Utilities Mfg. Co.*, 264 Fed. 470 (C. C. A. 8th, 1920); *Philadelphia Storage Battery Co. v. Kelly-How-Thomson Co.*, 64 F. (2d) 834 (C. C. A. 8th, 1933); *Sallies v. Johnson*, 85 Conn. 77, 81 Atl. 974 (1911); *Hobaica v. Byrne*, 123 Misc. 107, 205 N. Y. Supp. 7 (Sup. Ct. 1924); *Herndon v. Durham & S. R. R.*, 161 N. C. 650, 77 S. E. 683 (1913); *Franklin Bond Corp. v. Smith*, 163 Okla. 70, 20 P. (2d) 912 (1933). In some states promises without an intent to perform are declared fraudulent by statute. CAL. CIV. CODE (Deering, 1937) §1710 (4).

⁵ *Bielby v. Bielby*, 333 Ill. 478, 165 N. E. 231 (1929); *Reed v. Cooke*, 331 Mo. 507, 55 S. W. (2d) 275 (1933); 5 WIGMORE, EVIDENCE (2d ed. 1923) §2439.

⁶ *Bernheimer v. First Nat. Bank of Beverly Hills*, 78 F. (2d) 139 (C. C. A. 9th, 1935); *United North and South Oil Co. v. Tiller*, 283 S. W. 676 (Tex. Civ. App. 1926); *Fox Film Corp. v. Ogden Theatre Co.*, 82 Utah 279, 17 P. (2d) 294 (1932); 5 WIGMORE, EVIDENCE (2d ed. 1923) §2413; 3 WILLISTON, CONTRACTS (rev. ed. 1937) §§631, 632.

fraudulent misrepresentations of present facts other than intent, or evidence of fraud in the execution of a written contract, is not within the purview of the parol evidence rule and may be shown by parol.⁷ In those jurisdictions that recognize as fraudulent a promise made with intent not to perform, no distinction is usually made between this misrepresentation of a state of mind and misrepresentations of more ordinary and more tangible species of fact, such as weight, color, dimensions, etc. The promise, being classified in the general category of fraud, may be shown by parol to vitiate the writing.⁸

Thus, in most jurisdictions a fraudulent promise is available at the option of the injured party as a defense to an action on the contract.⁹ The parties may not prevent extrinsic proof of the fraud by inserting a stipulation to the effect that the written agreement contains all representations and a full and final statement of the terms of bargain,¹⁰ though the contract may be made incontestable for fraud after the lapse of a specified period of time.¹¹ Further, the fraudulent promise is a defense to a suit for specific performance of the written contract;¹² or it may be made the basis of a suit for rescission of the contract.¹³ In an action of deceit for damages suffered from the promise, most courts allow the introduction of evidence of the fraudulent promise on

⁷ *Tyler v. Anderson*, 106 Ind. 185, 6 N. E. 600 (1886); *White v. Fisheries Products Co.*, 185 N. C. 68, 116 S. E. 169 (1923); *Ziliox v. City View Apt. & Storage Co.*, 20 Ohio App. 156, 153 N. E. 183 (1925); *Hooker v. Wilson*, 69 Okla. 43, 169 Pac. 1097 (1918); *Middleton v. Brawley*, 12 S. W. (2d) 257 (Tex. Civ. App. 1928).

⁸ *Knudson v. Domestic Utilities Mfg. Co.*, 264 Fed. 470 (C. C. A. 8th, 1920); *Philadelphia Storage Battery Co. v. Kelly-How-Thomson Co.*, 64 F. (2d) 834 (C. C. A. 8th, 1933); *Sallies v. Johnson*, 85 Conn. 77, 81 Atl. 974 (1911); *Franklin Bond Corp. v. Smith*, 163 Okla. 70, 20 P. (2d) 912 (1933).

⁹ *Neff & Frey Co. v. Ashmead*, 36 F. (2d) 771 (C. C. A. 2d, 1929); *Holt v. Quaker State Oil Refining Co.*, 67 F. (2d) 170 (C. C. A. 4th, 1933); *Hunt v. Field, Inc.*, 202 Cal. 701, 262 Pac. 730 (1928); *Moore v. Harmon*, 142 Ind. 555, 41 N. E. 599 (1895); *National Equipment Corp. v. Volden*, 190 Minn. 596, 252 N. W. 444 (1934); *Voliva Hardware Co. v. Kinion*, 191 N. C. 218, 131 S. E. 579 (1926); *Diamond Rubber Co. v. Feldstein*, 11 N. J. Misc. 457, 166 Atl. 710 (Sup. Ct. 1933); *Machim v. Prudential Trust Co.*, 210 Pa. 253, 59 Atl. 1073 (1904); *Clem v. Evans*, 286 S. W. 273 (Tex. Civ. App. 1926); *Stevens v. Lintwood Drug Co.*, 155 Va. 353, 154 S. E. 515 (1930).

¹⁰ *Howie Bros. v. Walter Platt & Co.*, 83 Miss. 15, 35 So. 216 (1903); *Margolis v. Pinna*, 99 N. J. L. 515, 124 Atl. 529 (1924); *Trinity Valley Trust Co. v. Stockwell*, 81 S. W. 793 (Tex. Civ. App. 1904); *Free Sewing Machine Co. v. S. T. Atkin Furniture Co.*, 71 S. W. (2d) 604 (Tex. Civ. App. 1934).

¹¹ *Columbian National Life Ins. Co. v. Wallerstein*, 91 F. (2d) 351 (C. C. A. 7th, 1937).

¹² *Gridley v. Tilson*, 202 Cal. 748, 262 Pac. 322 (1928); *Florimond Realty Co. v. Wayne*, 268 Mass. 475, 167 N. E. 635 (1929); *Lovejoy v. MacKinnon*, 52 R. I. 203, 159 Atl. 736 (1932); see *Lozier v. Janss Investment Co.*, 1 Cal. (2d) 666, 667, 36 P. (2d) 620, 621 (1934).

¹³ *Stewart v. Crowley*, 213 Cal. 694, 3 P. (2d) 562 (1931); *Logan v. Collinson*, 114 Kan. 620, 220 Pac. 291 (1923); *Hill v. Maguire*, 19 La. App. 798, 140 So. 169 (1932); *Feuerstein v. New Century Realty Co.*, 304 Pa. 271, 156 Atl. 110 (1931).

the ground that the parol evidence rule has no application in a tort action.¹⁴

However, as indicated by the principal case, a few jurisdictions, though recognizing that a promise made without intent to perform is fraudulent, have in some measure restricted the parol proof of such a promise. The California court declares that where the fraud sought to be proved is predicated on such a promise, and the promise is contradicted by the terms of the subsequently executed written contract, of which terms the promisee is fully cognizant, parol evidence is not admissible to show the fraud in either contract or tort actions.¹⁵ This view has been approved in Texas.¹⁶ An even greater distrust of parol evidence is exhibited by Massachusetts,¹⁷ where the courts decline to allow the introduction of evidence of *any* fraudulent misrepresentation where the alleged misrepresentation is contradicted by the subsequent writing, or where the subject matter of the misrepresentation is entirely omitted from the writing.

In working out these various degrees of restriction, or lack of restriction, on the admissibility of parol evidence of fraud to vitiate a written contract, all courts seek a common goal—the promulgation of a general rule that will attain substantial justice in the greatest number of individual cases. The conflict between them as to what rule will best attain that end is a result of the clash between two universally recognized concepts: (1) that, as the final written agreement is ordinarily the best evidence of what actually occurred between the parties, the integrity of written instruments should be preserved against encroachment by parol testimony;¹⁸ (2) that a writing should not be permitted to act as a shield for a wrongdoer.¹⁹ Evaluated in the light of these broad principles, the Massachusetts rule seems unnecessarily

¹⁴ *Schuster v. North American Hotel Co.*, 106 Neb. 672, 186 N. W. 87 (1921); *Voliva Hardware Co. v. Kinion*, 191 N. C. 218, 131 S. E. 579 (1926); *Miller v. Troy Laundry Machinery Co.*, 178 Okla. 313, 62 P. (2d) 975 (1936); *Trotter v. Williams*, 167 Wash. 151, 8 P. (2d) 980 (1932).

¹⁵ *Tockstein v. Pacific Kissel Kar Branch*, 32 Cal. App. 262, 164 Pac. 906 (1917); *Yuba Mfg. Co. v. Stone*, 39 Cal. App. 440, 179 Pac. 418 (1919); *Campbell v. Sears, Roebuck & Co.*, 136 Cal. App. 765, 29 P. (2d) 910 (1934); *Bank of America National Trust and Savings Ass'n v. Pendergrass*, 4 Cal. (2d) 258, 48 P. (2d) 659 (1935); see *Lindemann v. Coryell*, 59 Cal. App. 788, 789, 212 Pac. 47, 48 (1923); cf. *Hunt v. Field, Inc.*, 302 Cal. 701, 262 Pac. 730 (1928).

¹⁶ *Wright v. Couch*, 54 S. W. (2d) 207 (Tex. Civ. App. 1932); *Cassel v. West*, 98 S. W. (2d) 437 (Tex. Civ. App. 1936); *Distributors Investment Co. v. Patton*, 110 S. W. (2d) 47 (Tex. Civ. App. 1937); *Mitcham v. London*, 110 S. W. (2d) 140 (Tex. Civ. App. 1937).

¹⁷ *Loughery v. Central Trust Co.*, 258 Mass. 172, 154 N. E. 583 (1927); *Orange County Co. v. Appleton*, 270 Mass. 123, 169 N. E. 783 (1930).

¹⁸ See 3 WILLISTON, *CONTRACTS* (rev. ed. 1936) §639; (1934) 28 ILL. L. REV. 717; (1934) 18 MINN. L. REV. 570.

¹⁹ See *Gross v. Stone*, 197 Atl. 137, 142 (Md. 1938); *Chadbourn and McCormick, The Parol Evidence Rule in North Carolina* (1930) 9 N. C. L. REV. 151.

harsh. By excluding evidence of any fraudulent representation contradicted by the writing, "clear and convincing" proof of fraud in the inducement may often be prevented from reaching the jury, thus shielding a wrongdoer.

However, consideration of the California rule (excluding evidence of a promise made with intent not to perform where the promise is contradicted by the subsequent writing) might well lead to the conclusion that this more narrow restriction is a desirable one. By reason of the necessarily intangible nature of proof of the promisor's state of mind, *i.e.*, that at the time he made the promise he intended not to keep it, "clear and convincing" proof of this type of fraud can seldom be presented. Often the jury must draw the inference of such an intent from little more than evidence of the making of the promise and the non-performance of it. In this situation the written contradiction of the alleged oral promise would seem the more reliable evidence, where the promisee knew the terms of the writing.²⁰ In allowing the introduction of only the more reliable evidence, California and Texas make a commendable return to the spirit of the parol evidence rule in the face of modern tendencies²¹ to render uncertain the finality of written instruments.

MARGARET CLOYD JOHNSON.

Corporate Reorganization—Bondholders' Committees—Fiduciary Obligations.

T executed a note secured by a pledge of securities, including bonds of the *Y* corporation in the amount of \$61,000, to the appellant bank. Subsequently, the *Y* corporation defaulted on its bonds and a bondholders' protective committee was formed to receive bond deposits in order to seek a reorganization. The cashier of the appellant bank became the most active member of this committee.¹ The *Y* bonds held by the bank as collateral security were deposited by agreement between it and *T*, and a certificate of deposit was assigned to the bank. *T* failed to make a payment on the note and all collateral security was sold, being bought by the bank as a sole bidder for \$5,000. On an attempt by the bank to prove a claim for the par value of the *Y* bonds in a proceeding in corporate reorganization, *held*, the bank acted under a fiduciary duty to the bondholders and was not entitled to profit from

²⁰ See (1936) 20 MINN. L. REV. 555.

²¹ 3 JONES, COMMENTARIES ON EVIDENCE (2d ed. 1926) §§1487, 1518; 3 WILLISTON, CONTRACTS (rev. ed. 1936) §634.

¹ The bank was treated as a member of the committee by the court in this case. This disregard of the corporate entity in holding that the position of the cashier was the position of the bank seems reasonable on the facts of the case.